# Under what circumstances may a tribunal grant security for costs in investment treaty arbitration? (Manuel García Armas v Venezuela)

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**Arbitration analysis: Elvezio Santarelli, a partner, and Monica Selvini, an associate, at Watson Farley & Williams, assess the impact of the security for costs decision in Manuel García Armas v Venezuela.**

*Manuel García Armas et al v Bolivarian Republic of Venezuela*, PCA Case No 2016-08—order dated 20 June 2018 (in Spanish)

## What are the practical implications of the decision?

In investment treaty arbitration proceedings, tribunals have generally rejected applications to issue orders for security for costs (OFSC). This case represents the second exception to this trend, following the August 2014 decision in *RSM Production Corporation v St Lucia* (ICSID Case No ARB/12/10).

The reasoning of the tribunal follows principles set out in previous investment treaty arbitration decisions that an OFSC will only be granted in exceptional circumstances and the existence of third-party funding (TPF) is not, per se, proof of the claimant's insolvency to potentially justify an OFSC.

The decision highlights the relevance of the claimants' solvency to such an application and clarifies the role of the TPF agreement and of the burden of proof when assessing the claimants' solvency. Indeed, the decision suggests that lack of adverse costs covered in a TPF agreement, combined with other relevant circumstances, may justify an OFSC.

## On what grounds was the application for security for costs made?

The respondent state applied for an OFSC of at least $US 5m under Article 26 of the 1976 UNCITRAL Arbitration Rules (the UNCITRAL Rules) and Article 46 of the ICSID Additional Facility Arbitration Rules, asserting that although the claimant had the benefit of TPF, it was clear that the funding agreement in question would not cover any adverse costs order in the proceedings and the claimant had not proven its solvency. Accordingly, it was said by the claimant that there was a real risk that the respondent would not recover its costs if the claim was determined in its favour.

## What did the tribunal decide and on what bases?

The tribunal granted an OFSC for $US 1.5m, noting the following.

- the applicable arbitration rules and the relevant Dutch procedural law empowered it to order interim measures, including an OFSC
- under Article 26 of the UNCITRAL Rules, tribunals may take any interim measure deemed necessary, provided that the measure relates to the subject matter of the dispute—the tribunal considered that an interim measure is necessary when:
  - it is, prima facie and without prejudging the final award, reasonably possible for the applicant to obtain a final award in its favour (and consequently, an order for costs)
  - there is a likelihood that, in the absence of an OFSC, the applicant would suffer damage that could not be adequately compensated for
  - the damage to the applicant in not making an OFSC would be greater than the damage to the counterparty in making an OFSC

- there is an urgency

The tribunal considered that all these factors were made out by the respondent in this case.

Attention was drawn to the assessment of the claimant's solvency. It was found that not all the claimants had assets which could be enforced against and there was no evidence of joint liability between the claimants. Further, while the presence of TPF did not establish that the claimants were automatically insolvent, the fact that adverse costs were not covered by the TPF agreement was a key factor in finding that there was a risk that the claimants would not be able to pay adverse costs.

While it is normally for the applicant to prove that the necessary requirements for an interim order are met, in this case, where the solvency of the claimants was of particular significance and given the complex nature of the evidence, the claimants were in a better position to produce such evidence, the tribunal considered that the burden of proof should fall on the party who had better access to the evidence.

The existence of TPF without cover for adverse costs, together with the issues regarding the claimants' solvency and their joint liability, constituted exceptional circumstances which justified the grant of an OFSC.

**Does the approach of the tribunal differ to that taken in ICSID arbitration cases?**

In the past, tribunals have rejected OFSC for several reasons. In *Emilio Agustin Maffezini v The Kingdom of Spain* (ICISD Case No. ARB/97/7), it was held that an OFSC could not be made as it provides protection for a contingent right (ie a right to recover costs which have not yet been assessed as falling due), while in *Victor Pey Casadi and President Allende Foundation v Republic of Chile* (ICSID Case No. ARB/98/2), it was held that the lack of expressed language in Article 47 of the ICSID Convention implied a presumption against OFSC and that there was no requirement for the claimant to prove its creditworthiness. In *Rachel S Grynberg, Stephen M. Grynberg, Miriam Z. Grynberg and RSM Production Company v Grenada* (ICSID Case No. ARB/10/6), it was held that the right to reimbursement of costs was protectable, but the tribunal doubted that an absence of assets alone would provide a sufficient basis for such an order. *RSM Production Corporation v Saint Lucia* (ICSID Case No. ARB/12/10) was the first investment treaty arbitration decision providing for an OFSC, the tribunal stating that such a measure is intended to protect the integrity of arbitration proceedings, even if the protected rights are contingent, including the protection of a procedural right such as the right to reimbursement of costs.

*RSM v Saint Lucia* suggested that the tribunal has an implied power under Article 47 of the ICSID Convention and Article 39(1) of the ICSID Arbitration Rules to protect the integrity of the arbitration and, through interim measures, the rights of the parties, both substantive and procedural. In *Eskosol S.p.A. in liquidazione v Italian Republic* (ICSID Case No. ARB/15/50), this was doubted on the basis that an application for OFSC is focused on the 'ability to obtain effective relief' and not on a right to receive reimbursement of costs. It would be curious if this could protect a respondent's right to collect on a costs award by making an OFSC where the enforcement of a final award is otherwise left to domestic enforcement law. *Armas* confirms that OFSC can be issued in arbitrations, that the decision in *RSM* was not a one off, and that, although tribunals are aware that such an interim measure protects a contingent right, a final award on costs may be useless if an OFSC is not made.

The decision also highlights the requirement of 'exceptional circumstances' necessary to grant an OFSC. In *Eskosol*, the existence of an after-the-event insurance policy which would meet an adverse costs order was sufficient to exclude the existence of exceptional circumstances in a claim in which the claim was supported by TPF. In *RSM v Saint Lucia,* the history of the claimant in not paying costs orders in previous disputes and the lack of certainty as to whether the TPF agreement covered

adverse costs led to a finding of exceptional circumstances. In *Armas*, the exceptional circumstances related to the fact the TPF agreement did not cover adverse costs and that there was insufficient evidence produced by the claimants to demonstrate their solvency and joint liability.

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